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FIRST DECLARATION OF RICHARD J. SAMUELS



## Table of Contents

I.	Qualifications .....	1
II.	Materials Given to Review and Question Posed .....	2
III.	General Discussion of the Academic Literature Relating to Such Groups as the Le Coane Group .....	3
IV.	Application of the General Principles to the Le Coane Group .....	7
V.	My Opinion .....	11
VI.	Jurat .....	12

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## I. Qualifications

(1) I am Ford International Professor at the Massachusetts Institute of Technology, where I am also Founding Director of the MIT Japan Program. I served as Head of the Department of Political Science between 1992 and 1997 and as vice-chairman of the Committee on Japan of the National Research Council from 1990 until 1996. In 1992 I was elected a member of the Council on Foreign Relations. In 1994 I became a member of the Abe Program Fellowship Committee of the Social Science Research Council. I am also an Associate in Research at the Reischauer Institute, Harvard University. From 1988 to 1993 I was a member of the Joint Committee on Japanese Studies of the American Council of Learned Societies and the Social Science Research Council. I have been awarded three Fulbright Fellowships and a National Science Foundation Research Grant to support four separate extended research trips to Japan, totaling six years in the field. In October 1998 I was awarded an Abe Fellowship for field research in Japan and Italy during 1999-2000.

(2) I have written or edited six books, most recently "Rich Nation, Strong Army": National Security and the Technological Transformation of Japan, Cornell University Press (1994), which won the 1996 John Whitney Hall Prize of the Association of Asian Studies and the 1996 Arisawa Memorial Prize of the Association of American University Presses. My 1987 book, The Business of the Japanese State: Energy Markets in Comparative and Historical Perspective (Cornell University Press) received the Masayoshi Ohira Memorial Prize in 1988. In 1983, Princeton University Press published my Politics of Regional Policy in Japan. I have also contributed essays and articles to The Cambridge Encyclopedia of Japan, International Organization, International Security, Daedalus, The Sloan Management Review, The Journal of Modern Italian Studies, and other journals. I am also a regular columnist for the Mainichi

Shimbun. In these publications I have explored the relationships between firms and the state in Japan, and I have paid careful attention to the relationships among firms at different levels of the value-added chain: manufacturers/suppliers, producers/distributors, etc.

- (3) I read and speak Japanese with professional proficiency.
- (4) I received my Ph.D. from the Massachusetts Institute of Technology, Department of Political Science in 1980, my MA from Tufts University in 1974, and my AB from Colgate University, magna cum laude, in June 1973.
- (5) A copy of my CV is the party Chao's Exhibit 1030.

## II. Materials Given to Review and Question Posed

- (6) Charles Gholz, counsel for the party Chao, gave me the following materials to review.
  - (a) the declaration of Masahiro Sudo and every exhibit referred to therein;
  - (b) the declaration of Yasuo Fukuwa and every exhibit referred to therein;
  - (c) the supplementation declaration of Yasuo Fukuwa and every exhibit referred to therein;
  - (d) a draft outline of cross-examination for Mr. Sudo;
  - (e) a draft outline of cross-examination for Mr. Fukuwa;
  - (f) transcripts of the depositions of Messrs. Sudo and Fukuwa; and
  - (g) a copy of the organizational document, or *kisoku*, of the Le Coane Group and the party Iwamoto's translation thereof, which is the party Chao's Exhibit 1060.

(7) Mr. Gholz asked for my opinion concerning the credibility of the assertions by Messrs. Sudo and Fukuwa that members of the Le Coane Group were under no obligation to keep matters discussed at group meetings confidential. In addition, Mr. Gholz asked me to critique his proposed lines of questions for Messrs. Sudo and Fukuwa and to suggest additional lines of questions. Although I have read the statements in the Sudo and Fukuwa declarations and in the transcripts of their depositions relating to the International Optical Fair in Tokyo, Mr. Gholz did not ask me for my opinion on those statements.

### **III. General Discussion of the Academic Literature Relating to Such Groups as the Le Coane Group**

(8) "Groups" such as the Le Coane Group have been frequently discussed in the academic literature and are very familiar to me. Such "vertical" business associations are quite common in Japanese commerce and industry. Sometimes referred to as "industry groups" (*kōgyōkai*) or as "supplier associations" (*kyōryōkukai*, which is literally translated as "cooperation groups"), these associations usually cluster around a single manufacturer. (Toyota's *kōgyōkai* is the most famous example). Sometimes they are associations of manufacturers and suppliers, and sometimes they are associations of manufacturers and distributors, as in the case of the Le Coane Group. Either way, they are not considered "open." Membership is by invitation only, and while neither the suppliers nor the distributors are expected to be entirely monogamous vis-à-vis the manufacturer, the expectation is that what is discussed and learned in their meetings will be kept "in-house."

(9) A great deal has been written about interfirm relationships in Japan. There is a pervasive sense and general agreement that Japanese firms are embedded in particularly dense

networks in which there is rather greater information exchange and coordination than neo-classical theory would predict or find efficient.

(10) For example, Imai<sup>1</sup> reports that "the dense, intricate, and overlapping interaction within the Japanese manufacturing and distribution system...creates advantages for Japanese suppliers in their speed and adaptability to continuous change in business environments..." (p. 179). The Japanese system requires "speedy coordination between marketing, production, and R&D..." (p.183).

(11) As noted above, these relationships are common among producers and distributors, as in the case of the Le Coane Group, as well as among producers and subcontractors. According to Nishiguchi,<sup>2</sup> the formal institutional ties between assemblers and suppliers help considerably to facilitate problem solving. He says that "Japanese subcontracting relations are characterized by an institutional design that aims at continuous quality improvement and cost reduction through problem solving-oriented commitments..." (p.181). For Nishiguchi, both final assemblers and suppliers benefit from the same sort of institutional commitment to "bilateral problem solving" across the value added chain that appears to characterize the Le Coane Group.

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<sup>1</sup>Imai, Kenichi, "Japanese Business Groups and the Structural Impediments Initiative," in K. Yamamura, ed. Japan's Economic Structure: Should it Change? Seattle: Society for Japanese Studies, 1990. A copy of Imai is the party Chao's Exhibit 1035.

<sup>2</sup>Nishiguchi, Toshihiro, Strategic Industrial Sourcing: The Japanese Advantage. New York: Oxford University Press, 1994. A copy of the title page, the copyright page, and chapter 6 of Nishiguchi is the party Chao's Exhibit 1034.

(12) An excellent characterization of the generic form of “cooperation groups” or “supplier associations” (*kyōryōkukai*) is offered by Mari Sako<sup>3</sup> of the London School of Economics. She explains that such interfirm organizations are ubiquitous among Japanese automobile manufacturers and that their stability affords members the opportunity to share technological and marketing information among themselves:

[The *kyōryōkukai*] is generally a voluntary association with their [sic; its] own rules and regulations. Its aim is generally to enhance member suppliers' cooperation with the assembler and with each other. Most of the assemblers' associations have a name which signifies cooperation, friendship, or prosperity. Some supplier associations, just like Japanese companies, are described as a “community of fate” (*unmei kyōdōtai*). [p.11.]

(13) Gerlach's<sup>4</sup> is the most comprehensive English language analysis of “intercorporate alliances” in Japan. Speaking primarily to the *keiretsu* alliances across market segments, Gerlach reports “a strong predilection for firms in Japan to cluster themselves into coherent groupings of affiliated companies...” (p. xiii). Importantly, he acknowledges that the now famous term “*keiretsu*” is inconsistently applied to (and masks) the fact that a wide variety

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<sup>3</sup>Sako, Mari, “Associations in the Japanese Automobile Industry: Collective Action for Technology Diffusion,” Paper presented to the 1995 Annual Sponsors Meeting, International Motor Vehicle program, Toronto. A copy of Sako's paper is the party Chao's Exhibit 1037.

<sup>4</sup>Gerlach, Michael, Alliance Capitalism: The Social Organization of Japanese Business. Berkeley: University of California Press, 1992. A copy of the title page, the copyright page, and Chapters I-III of Gerlach is the party Chao's Exhibit 1036.

of alliances exist in Japan. These alliances each display some degree of the following characteristics which combine to form "the social structure of markets" in Japan:

- (a) affiliational ties which are less binding than vertical integration but more binding than arm's length transactions;
- (b) long term relationships which are more diffuse than contractual ones;
- (c) multiplex relationships in which capital ties may be only one of several kinds of formal ties;
- (d) extended networks in which the parties formally associate can facilitate relationships to other related firms; and
- (e) symbolic ties which bind even in the absence of legal arrangements.

(14) Gerlach points out that a great deal of Japanese business is transacted "outside" the formal confines of firms. Much has been delegated to interfirm institutions—"localized networks of long-term mutual obligation... [and] preferential trading." (p.66). Of particular relevance for the case at hand:

the Japanese distribution system works largely through external networks. Within domestic markets, wholesalers (*ton 'ya*) are organized into elaborate networks in which products may pass through three or four middle stages before reaching final users. [p. 63.]

(15) Gerlach insists that Japanese business transactions "can be dimensionalized along a continuum from 'relational' to 'transactional' exchange." (p.70). He contrasts the one time transaction between anonymous parties to the differentiating feature of Japanese business

practice—the “relational” exchange in which “actors rely upon various forms of implicit assumptions and agreements to organize their relationships. (p.70).

(16) Here Gerlach is echoing Ronald Dore's<sup>5</sup> seminal analysis of Japanese business relationships. Dore focuses upon “goodwill”—“the sense of diffuse personal obligation which accrue between individuals engaged in recurring contractual economic exchange.” (p.170). Dore asserts that this “sense of diffuse personal obligation” is the “primordial embodiment of basic social bonds” (p. 171) of Japanese capitalism. Noting that “benevolence” was rejected as an economic motive by Adam Smith, Dore argues that “goodwill” is a critical element in Japanese economic behavior. Opportunism is reduced by the stability of relationships among economic actors, relationships that both sides recognize the obligation to maintain. Thus, “relational contracting” (which he compares to a “marriage”) is much more common in Japan than “spot contracting” (which he compares to a “one-night stand”). Thus firms persist in stable relationships—elsewhere compared to “extended family groupings”—and agree to share the costs of bad times and the gains of good times. The material gains are not insignificant for Dore: trust and mutual dependency beget a more rapid flow of information and hence greater flexibility and nimbleness in the marketplace.

#### **IV. Application of the General Principles to the Le Coane Group**

(17) As I said at the outset, I read and speak Japanese proficiently, and I have read all of the Japanese language materials concerning the meeting of the Le Coane Group referred in the declarations of Messrs. Sudo and Fukuwa, not just the selected excerpts translated by the party

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<sup>5</sup>Dore, Ronald, “Good Will and the Spirit of Market Capitalism,” in Taking Japan Seriously: A Confucian Perspective Leading Economic Issues, Stanford: Stanford University Press, 1987. A copy of Dore is the party Chao's Exhibit 1033.

Iwamoto, and I have read the organizational document (or *kisoku*) of the Le Coane Group in the original Japanese. Having done so, it is my opinion that the Le Coane Group is a Pentax-sponsored forum for the exclusive interaction between Pentax and its distributors. While there is no evidence that Pentax has capital ties with these firms, the minutes (*gijiroku*) of the "Second Meeting of Sales Representatives of the Le Coane Group" suggest that the activities of this group were very collaborative. Sales and marketing representatives met "to continue sales cooperation while overcoming common problems each firm had with the price, design, and low brand recognition of the 'Le Coane Eman' line" of eye wear. Those representatives discussed market conditions and plans for sales promotions, and the Pentax representatives solicited suggestions for marketing the Le Coane Eman product line from the non-Pentax representatives. Representatives of Pentax and its distributors discussed a jointly administered questionnaire to determine the prospects for particular styles and products, and they renewed the tenure of the members of a "development committee."

(18) That the Le Coane Group's name is the same as the product line being promoted by Pentax suggests that this is more than a merely voluntary association of firms that might come and go. It suggests that this is a close-knit group of firms dedicated to the collaborative promotion, marketing, and sales of a particular product line. According to the minutes, representatives of Pentax and its distributors work together to identify common problems and their solutions. The "Le Coane Group" (*kai*) is a problem-identifying and problem-solving group comprising distributor firms and Pentax. That it is also referred to in the minutes as the "Le Coane Company" (*sha*) suggests an even closer association than is customary with such groups.

(19) Incidentally, the party Iwamoto's translation of the organizational document (or

*kisoku*) for the Le Coane Group contains two major errors.

(20) The first major error in the translation of the *kisoku* is that the translator called the Le Coane Group the Le Coane Company throughout the translation. However, in the Japanese, only the word "kai" (group) is used. The word "sha" (company) never appears.

(21) The second mistake in the translation is more significant . In the Japanese, the non-Pentax members of the Le Coane Group are called "regular members," and they pay 10,000 yen (approximately \$85.00) per month to belong to the Le Coane Group. Pentax, on the other hand, is the only "special member" of the Le Coane Group, and it pays 100,000 yen (approximately \$850.00) per month to belong to the Le Coane Group. The translation has it backwards, making it look as if the distributors are bearing the bulk of the burden of the costs of running the Le Coane Group. To the contrary: Pentax pays for most of the costs, and it is the site of the secretariat to boot. Moreover, it is Pentax employees who prepare the minutes, arrange the meetings, set the agenda, etc. Pentax is clearly in charge here.

(22) I read with great interest Mr. Fukuwa's statement that the designation Le Coane *sha* is reserved for the French company. Having read that I went back and re-read the minutes. In that document, the word "sha" appears only once, in the untranslated paragraph 9. It seemed clear to me on my initial reading (and it still seems clear to me upon re-reading that paragraph with Mr. Fukuwa's testimony in mind) that that paragraph refers to the Pentax-sponsored *kyōryōkukai* and not to any French company! Thus, my earlier impression that the interchangeable use of the two terms "kai" and "sha" implies a close "in-house-relationship" between Pentax and the *kyōryōkukai* is reinforced.

(23) I thought particularly telling Mr. Sudo's reaction to Mr. Gholz's question about whether he would feel free to disclose to a foreign competitor a Pentax disclosure to the Le

Coane Group that Pentax was going to introduce a new product to the next meeting of the IOFT.

As Mr. Sudo said, so doing would be dishonorable. Thus, even Mr. Sudo recognized and admitted that the information conveyed to the members of the Le Coane Group by Pentax was subject to important "strings" of confidentiality.

(24) As for Mr. Fukuwa's testimony, his professed confusion over the two meanings of the word *kyōryoku* (strong or powerful and a cooperative association) was startling -- and unbelievable. It is true that "*kyōryoku*" means "strong" when written with a different first character. However, when it is written that way, it is not combined with "*kai*" to refer to a group. Moreover, the word *kyōryokukai* is a familiar Japanese business term. In my opinion, it is totally unbelievable that Mr. Fukuwa did not know what Mr. Gholz was asking about.

(25) I also think that Mr. Fukuwa's admission that there are no public announcements of the meetings of the Le Coane Group supports my opinion that the Le Coane Group is a closed group. (Of course, that answer was exactly what I expected. That is how *kyōryokukai* work.)

(26) With respect to the exchange on page 60 of the transcript of Mr. Fukuwa's deposition, I wonder whether Mr. Fukuwa understood the question. I find it hard to believe that the Le Coane Group is the only *kyōryokukai* organized and run by Pentax. As is well known, Pentax is a large company with many products -- cameras being perhaps the best known in this country. I would expect that Pentax sponsors other *kyōryokukai*. It is a common (if not the modal) form of interaction among vertically related firms in Japan, some with a company and its sub-contractors and others with a company and its distributors.

(27) Finally, Mr. Fukuwa's claim (on page 71 of the transcript of his deposition) that the non-Pentax members of the Le Coane Group never tell Pentax anything confidential seems disingenuous to me. The non-Pentax members of the Le Coane Group are in that group to build

trust between themselves and Pentax, and sharing confidential information is a tried and true way to do that -- in Japan as in the United States.

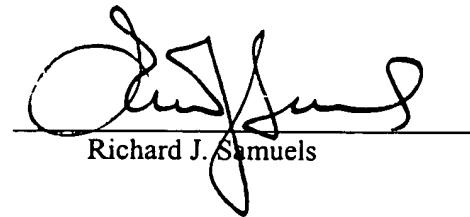
## V. My Opinion

(28) In my opinion, the statements by Messrs. Sudo and Fukuwa that the members of the Le Coane Group were under no obligation to keep matters discussed at group meetings confidential is, at the very least, misleading. It may well be that there was no written contract, articles of incorporation, or the like which contained an express obligation of secrecy. However, given the customs and traditions of Japanese business, no such express written contract or the like was necessary or expected. There was probably no express written contract, articles of incorporation, or the like that required the representatives of the distributors to wear clothes when they attended meetings of the Le Coane Group. However, just as it was clearly understood that the members of the Le Coane Group would wear clothes when they came to meetings, it was clearly understood that they would maintain in confidence anything that they learned at those meetings about Pentax's business plans, new products, and the like. Any non-Pentax company member of the Le Coane Group who "leaked" any such business-sensitive information could expect to be promptly "cut" from the group, and any individual representative of any member of the Le Coane Group (i.e., either any representative of Pentax or any representative of any non-Pentax member of the Le Coane Group) who "leaked" any such business-sensitive information could expect to be severely reprimanded by his or her company (presuming, of course, that the "leak" was not authorized). As has been written many, many times, many things that have to be expressed in contractual form in the United States do not have to be "put in writing" in Japan. That, however, does not mean that such things are not clearly understood by all.

VI. Jurat

(29) I declare under penalty of perjury under the laws of the United States of America that the foregoing is true and correct.

Date: 23 January 1999



Richard J. Samuels

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